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The ECA's Statement of Assurance provided to the European Parliament and the Council – independent auditor's report

(C/2023/112)

Opinion

I. We have audited:

(a) the consolidated accounts of the European Union, which comprise the consolidated financial statements [1] and the budgetary implementation reports [2] for the financial year ended 31 December 2022, approved by the Commission on 28 June 2023;

(b) the legality and regularity of the underlying *transactions*, as required by Article 287 of the Treaty on the Functioning of the European Union (TFEU).

Reliability of the accounts

Opinion on the reliability of the accounts

II. In our opinion, the consolidated accounts of the European Union (EU) for the year ended 31 December 2022 present fairly, in all material respects, the EU's financial position as at 31 December 2022, the *results* of its operations, its cash flows and the changes in its net assets for the year then ended, in accordance with the Financial Regulation and with accounting rules based on internationally accepted accounting standards for the public sector.

Legality and regularity of the transactions underlying the accounts

Revenue

Opinion on the legality and regularity of revenue

III. In our opinion, the revenue underlying the accounts for the year ended 31 December 2022 is legal and regular in all material respects.

Expenditure

IV. For 2022, we continue providing two separate opinions on the legality and regularity of expenditure. This reflects the fact that the *Recovery and Resilience Facility (RRF)* is a temporary instrument delivered and financed in a way that is fundamentally different to normal budget spending under the multiannual financial framework (MFF).

Adverse opinion on the legality and regularity of budget expenditure

V. In our opinion, owing to the significance of the matter described under 'Basis for adverse opinion on the legality and regularity of budget expenditure', the budget expenditure accepted in the accounts for the year ended 31 December 2022 is materially affected by error.

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[1] Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union amending Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, and Decision No 541/2014/EU and repealing Council Regulation (EC, Euratom) No 966/2012 (OJ L 193, 30.7.2018, p. 1), Article 243.

[2] *Ibid.*, Article 244.

Qualified opinion on the legality and regularity of RRF expenditure

VI. In our opinion, except for the effects of the matters described under the 'Basis for qualified opinion on the legality and regularity of RRF expenditure', the RRF expenditure accepted in the accounts for the year ended 31 December 2022 is legal and regular in all material respects.

Basis for opinion

VII. We have conducted our audit in accordance with the International Federation of Accountants (IFAC) International Standards on Auditing (ISAs) and Codes of Ethics and the INTOSAI International Standards of Supreme Audit Institutions (ISSAIs). Our responsibilities under these standards and codes are described in more detail in the 'Auditor's responsibilities' section of our report. In that section, we also provide more information on the basis for our opinion on revenue (see paragraph ***XXXV***) and RRF expenditure (see paragraph ***XXXVII***). We have also met independence requirements and fulfilled our ethical obligations under the International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinions.

Basis for adverse opinion on the legality and regularity of budget expenditure

VIII. Our overall estimated level of error for budget expenditure accepted in the accounts for the year ended 31 December 2022 is 4,2 %. A substantial proportion of this expenditure is materially affected by error. This mainly concerns reimbursement-based expenditure, in which the estimated level of error is 6,0 %. Such expenditure increased to EUR 110,1 billion in 2022, representing 66,0 % of our audit population ([3]). The effects of the errors we found are therefore both material and pervasive to the year's accepted expenditure.

Basis for qualified opinion on the legality and regularity of RRF expenditure

IX. Eleven out of the 13 RRF payments (and related clearings of pre-financing) were affected by quantitative findings. Six of these payments were affected by material error. We also identified cases of weak design in the measures and underlying milestones or targets and problems with the reliability of information that member states included in their management declaration. Based on these elements, we consider that the overall effects of our findings are material, but not pervasive to the year's accepted RRF expenditure.

Key audit matters

We assessed the liability for pension and other employee benefits

X. The EU balance sheet includes a liability for pension and other employee benefits amounting to EUR 80,6 billion at the end of 2022 (2021: EUR 122,5 billion).

XI. Most of the liability for pension and other employee benefits relates to the Pension Scheme of Officials and Other Servants of the European Union (PSEO), amounting to EUR 73,1 billion (2021: EUR 109,7 billion). The liability recorded in the accounts is an estimate of the present value of expected future payments the EU will have to make to settle its pension obligations.

XII. The benefits paid under the pension scheme are charged to the EU budget. While the EU has not created a dedicated pension fund to cover the cost of future pension obligations, member states jointly guarantee the payment of the benefits, and officials contribute one third of the cost of financing the scheme. Eurostat calculates this liability annually on behalf of the Commission's accounting officer, using parameters such as the age profile and life expectancy of EU officials and assumptions about future economic conditions. These parameters and assumptions are also assessed by the Commission's actuarial advisors.

([3]) We provide further information in our 2022 annual report, paragraphs ***1.22***-***1.26***.

XIII. The decrease in the pension liability in 2022 is mainly due to the increase in the nominal discount rate, which is affected by rising global interest rates ([4]).

XIV. The second largest part of the liability for pension and other employee benefits is the EU's estimated liability towards the Joint Sickness Insurance Scheme (JSIS), which amounted to EUR 5,7 billion at the end of 2022 (2021: EUR 10,3 billion). This liability relates to EU staff members' healthcare costs payable during post-activity periods (net of their contributions).

XV. As part of our audit, we assess the actuarial assumptions made for these schemes and the resulting valuation. We base our evaluation on work carried out by external, independent actuarial experts. We check the basic data underlying the calculations, the actuarial parameters and the calculation of the liability. We also examine the presentation of the liabilities in the consolidated balance sheet and the notes to the consolidated financial statements.

XVI. We conclude that the estimate of the overall liability for pension and other employee benefits is presented fairly in the consolidated annual accounts.

We assessed significant year-end estimates presented in the accounts

XVII. At the end of 2022, the estimated value of incurred eligible expenses due to beneficiaries but not yet claimed was EUR 148,7 billion (2021: EUR 129,9 billion). These amounts were recorded as accrued expenses ([5]).

XVIII. The increase in that estimate relates mainly to the RRF, which is the centrepiece of *NextGenerationEU* (NGEU), the temporary recovery instrument aimed at helping to repair the immediate economic and social damage brought about by the COVID-19 pandemic. Payments to member states under this facility follow a predefined instalment profile up to 2026. At the end of 2022, accrued RRF expenditure amounted to EUR 22,6 billion (2021: EUR 12,3 billion).

XIX. In order to assess these year-end estimates, we examined the system the Commission had set up for the cut-off calculations to ensure its correctness and completeness in the directorates-general where most expenses were incurred. During our audit work on the sample of invoices and pre-financing payments, we examined the relevant cut-off calculations in order to address the risk of accruals being misstated. We sought clarification from the Commission's accounting services on the general methodology for establishing these estimates.

XX. We conclude that the estimate of the overall amount of accrued charges and other advances paid to member states is presented fairly in the consolidated annual accounts.

We reviewed the asset generated by the UK's withdrawal process

XXI. On 1 February 2020, the United Kingdom (UK) ceased to be an EU member state. Under the withdrawal agreement, the UK has committed to honouring all financial obligations under previous MFFs arising from its EU membership.

XXII. Following the end of transition period at 31 December 2020, further mutual obligations on the part of the EU and the UK give rise to certain liabilities and receivables for the EU. These obligations must be reflected in the EU's annual accounts. The Commission estimated that, at the balance sheet date, the EU accounts showed a net receivable due from the UK of EUR 23,9 billion (2021: EUR 41,8 billion), of which it is estimated that EUR 9,1 billion will be paid in the 12 months following the reporting date.

([4]) 2022 EU annual accounts, note 2.9.
([5]) These comprise accrued charges of EUR 85,9 billion on the liabilities side of the balance sheet and, on the assets side, EUR 62,8 billion reducing the value of pre-financing.

XXIII. As part of our normal audit procedures, we discussed with the Commission the timing, accuracy and completeness of the asset recognised and payments made. We recalculated the amounts concerned, reconciled them with the underlying records and checked the appropriateness of any assumptions used.

XXIV. We conclude that the estimate of the total asset recognised in relation to the UK's withdrawal process is presented fairly in the consolidated annual accounts.

We assessed impact on the accounts of Russia's war of aggression against Ukraine

XXV. On 24 February 2022, Russia invaded Ukraine. As the EU provides assistance to Ukraine in the form of loans and grants, we assessed the Commission's calculations concerning the EU's associated financial risk exposure, as well as their underlying basis, to ensure that the actual and potential consequences were reflected appropriately in the EU accounts. We assessed the Commission's calculations against our own and against existing data on the matter.

XXVI. We conclude that the treatment of the impact of Russia's war of aggression against Ukraine on the consolidated accounts is presented fairly in the consolidated annual accounts.

We assessed the impact of NGEU on the accounts

XXVII. With NGEU, the EU mobilised substantial means to reinforce the member states' public health sectors and mitigate the pandemic's socio-economic impact in the EU. To fund NGEU, the European Commission raises debt in the capital markets. These funds are being made available to the member states in the form of non-repayable grants or loans up to a previously agreed allocation. These activities have a significant effect on the financial statements. The most significant part of NGEU is the RRF.

XXVIII. As part of our normal audit procedures, we audited the assets, liabilities, revenue and expenses, including those related to NGEU. We conclude that they are presented fairly in the consolidated annual accounts.

Other matters

XXIX. Management is responsible for providing 'other information'. This term encompasses the 'Financial highlights of the year', but not the consolidated accounts or our report on these. Our opinion on the consolidated accounts does not cover this other information, and we do not express any form of assurance conclusion on it. Our responsibility in connection with the audit of the consolidated accounts is to read the other information and consider whether it is materially inconsistent with the consolidated accounts or the knowledge we have obtained in the audit or otherwise appears to be materially misstated. If we conclude that the other information is materially misstated, we are required to report this accordingly. We have nothing to report in this regard.

Responsibilities of management

XXX. In accordance with Articles 310 to 325 of the TFEU and with the Financial Regulation, management is responsible for preparing and presenting the EU's consolidated accounts on the basis of internationally accepted accounting standards for the public sector, and for the legality and regularity of the underlying transactions. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and presentation of financial statements that are free from material misstatement, whether due to *fraud* or error. Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities (laws, regulations, principles, rules and standards) which govern them. The Commission is ultimately responsible for the legality and regularity of the transactions underlying the EU's accounts (Article 317 of the TFEU).

XXXI. When preparing the consolidated accounts, management is responsible for assessing the EU's ability to continue as a going concern, disclosing any relevant matters and using the going concern basis of accounting unless it either intends to liquidate the entity or cease operations, or has no realistic alternative but to do so.

XXXII. The Commission is responsible for overseeing the EU's financial reporting process.

XXXIII. Under the Financial Regulation (Title XIII), the Commission's accounting officer must present for audit the consolidated accounts of the EU first as provisional accounts by 31 March of the following year and as final accounts by 31 July. The provisional accounts should already give a true and fair view of the EU's financial position. It is therefore imperative that all items of the provisional accounts are presented as final calculations, allowing us to perform our task in line with (Title XIII) of the Financial Regulation and by the given deadlines. Any changes between the provisional and final accounts would normally result from our observations only.

Auditor's responsibilities for the audit of the consolidated accounts and underlying transactions

XXXIV. Our objectives are to obtain reasonable assurance as to whether the EU's consolidated accounts are free from material misstatement and the underlying transactions are legal and regular and on the basis of our audit, to provide the European Parliament and the Council with a statement of assurance as to the reliability of the accounts and the legality and regularity of the underlying transactions. Reasonable assurance is a high level of assurance, but it is not a guarantee that the audit has necessarily detected all instances of material misstatement or non-compliance that may exist. These can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence any economic decisions taken on the basis of these consolidated accounts.

XXXV. For revenue, our examination of VAT and GNI-based own resources takes as its starting point the macroeconomic aggregates from which these are calculated, and assesses the Commission's systems for processing these up to the point at which the member states' contributions have been received and recorded in the consolidated accounts. For the own resource based on non-recycled plastic packaging waste, we review the process for compiling forecast data and the Commission's controls on the calculation of member states' contributions based on this data, up to the point the revenue amounts were received and recorded in the accounts. For traditional own resources, we examine the customs authorities' accounts and analyse the flow of duties up until the amounts have been received by the Commission and recorded in the accounts. Customs duties are at risk of either not being declared or being declared incorrectly to the national customs authorities by importers. The actual import duties collected will therefore fall short of the amount that should theoretically be collected. This difference is known as the 'customs gap'. These evaded amounts are not captured in member states' TOR accounting systems and do not fall within the scope of our audit opinion on revenue.

XXXVI. For expenditure, we examine payment transactions once expenditure has been incurred, recorded and accepted. This examination covers all categories of payments at the point they are made, except advances. We examine advance payments once the recipient of funds has provided evidence of their proper use and the institution or body has accepted that evidence by clearing the advance payment, which might not happen until a subsequent year.

XXXVII. For RRF expenditure, unlike other budget expenditure, the main condition for payment is the satisfactory fulfilment of predefined milestones or targets. Consequently, our audit focuses on whether the payment conditions and horizontal eligibility conditions were met. As compliance of expenditure incurred by final recipients with EU and national rules is not a condition for RRF payments, our audit does not involve a systematic assessment of this aspect. The RRF Regulation does not stipulate further criteria on how to interpret the word 'satisfactory', and, therefore, leaves the Commission with broad discretion when assessing the satisfactory fulfilment of milestones and targets. The assessment of qualitative achievements requires several judgements to be made, leading to different possible interpretations. This risk is particularly present when milestones or targets are vaguely designed.

XXXVIII. We exercise professional judgement and maintain professional scepticism throughout the audit. We also:

(a) Identify and assess the risks of material misstatement of the consolidated accounts and of material non-compliance of the underlying transactions with the requirements of EU law, whether due to fraud or error. We design and perform audit procedures responsive to those risks and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. Instances of material misstatement or non-compliance resulting from fraud are more difficult to detect than those resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Consequently, there is a greater risk of such instances not being detected.

(b) Obtain an understanding of internal control relevant to the audit in order to design appropriate audit procedures, but not for the purpose of expressing an opinion on the effectiveness of the internal control.

(c) Evaluate the appropriateness of the accounting policies used by management and the reasonableness of management's accounting estimates and related disclosures.

(d) Conclude as to the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, as to whether material uncertainty exists owing to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that such material uncertainty exists, we are required to draw attention in our report to the related disclosures in the consolidated accounts or, if these disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our report. However, future events or conditions may cause the entity to cease to continue as a going concern.

(e) Evaluate the overall presentation, structure and content of the consolidated accounts, including all disclosures, and assess whether the consolidated accounts fairly represent the underlying transactions and events.

(f) Obtain sufficient appropriate audit evidence regarding the financial information on the entities covered by the EU's scope of consolidation to express an opinion on the consolidated accounts and the underlying transactions. We are responsible for directing, supervising and carrying out the audit, and are solely responsible for our audit opinion.

XXXIX. We communicate with management regarding, among other matters, the planned scope and timing of the audit and significant audit observations, including any significant deficiencies in internal control.

XL. Of the matters discussed with the Commission and other audited entities, we determine which were of most significance in the audit of the consolidated accounts and are therefore the key audit matters for the current period. We describe these matters in our report unless law or regulation precludes public disclosure or, as happens extremely rarely, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh any public interest benefits.

20 July 2023

Tony MURPHY

President

European Court of Auditors

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